LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS

200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
http://www.in.gov/legislative

FISCAL IMPACT STATEMENT

LS 7078 | **NOTE PREPARED:** Apr 10, 2005
BILL NUMBER: HB 1083 | **BILL AMENDED:** Apr 8, 2005

SUBJECT: Taxation.

FIRST AUTHOR: Rep. Murphy | **BILL STATUS:** 2nd Reading - 2nd House
FIRST SPONSOR: Sen. Alting

FUNDS AFFECTED: X **GENERAL** | **IMPACT:** State & Local
X **DEDICATED**
FEDERAL

Summary of Legislation: (Amended) The bill postpones the expiration of the Earned Income Tax Credit until December 31, 2011.

The bill authorizes Marion County to increase it's County Option Income Tax rate by not more than 0.3%.

It provides that County Option Income Tax distributions for counties that increase the rate of the tax are adjusted in the immediately following calendar year.

It also legalizes and validates any ordinance or resolution adopted in Marion County to increase the County Option Income Tax rate by not more than 0.3%.

Effective Date: (Amended) Upon passage; May 15, 2005; July 1, 2005.

Explanation of State Expenditures: (Revised) *Earned Income Tax Credit (EITC) Extension:* The refundable portion of the EITC that goes to participants in the Temporary Assistance to Needy Families (TANF) Program qualifies as maintenance of effort (MOE) expenditures and contributes toward the state's annual MOE requirement under the TANF Program. It is estimated that refunds of the 6% EITC could potentially total about $8.0 M to $10.0 M annually. This is based on a simulation utilizing state taxpayer data and federal Earned Income Credit (EIC) data.

Distribution Adjustment: Under current law, when a county adopts a local option income tax (LOIT), the Department of State Revenue makes a distribution in the immediate year. The State Budget Agency must project a six-month balance in order to generate a recommendation on the certification for the newly adopting county. The bill would require the Budget Agency to make projections for counties with COIT that raise their rates, so that the Department would be able to adjust their certified distribution in the immediately following year for the rate increase. Under current law, a rate increase takes two years to reflect in a county's certified distribution. Certified distributions would begin to be affected, under the bill, in CY 2006. Differences in projections over the actual collections in a county that increased it's tax rate would be temporarily made up by the state General Fund and would be repaid with future COIT collections.

The provision would increase the administrative time necessary for the Budget Agency and the Department to project and certify new distributions for counties increasing their LOIT rates.

Explanation of State Revenues: (Revised) *Earned Income Tax Credit (EITC) Extension:* The current EITC is equal to 6% of the Federal Earned Income Credit (EIC), but is scheduled to sunset on December 31, 2005. The bill changes the sunset date for the EITC to December 31, 2011. Since the extension of the EITC would begin in tax year 2006, the revenue impact of the extension would begin in FY 2007. It is estimated that the annual revenue loss to the Individual Adjusted Gross Income (AGI) Tax could potentially be $49.7 M in FY 2007, $52.0 M in FY 2008, and $54.4 M in FY 2009.

Under current statute (with the December 31, 2005, sunset date), the EITC is estimated to reduce AGI Tax revenue by $45.4 M in FY 2005 and $47.5 M in FY 2006, with no revenue loss beginning in FY 2007. The FY 2005 and FY 2006 revenue loss is attributable to credits claimed for purposes of tax years 2004 and 2005, respectively. State tax return data for 2003 indicates that the EITC has very little impact on withholdings during the tax year due to advanced credit payments. Federal income tax data for tax year 2002 indicates that the federal EIC was claimed by 414,869 federal income tax filers residing in Indiana. This total was 11.0% above the 2001 total. The credits claimed in 2002 totaled about $692.0 M, increasing by about 13.2% over 2001 credits claimed. Annual growth in credits claimed by Indiana filers averaged 4.6% from 1996 to 2002.

Explanation of Local Expenditures: (Revised) *Marion County COIT:* The Marion County Income Tax Council would be allowed to adopt an ordinance to raise the County Option Income Tax rate by 0.3% to the maximum allowable rate of 1.00% in one year. The Council would likely be able to adopt an ordinance within existing resources.

Explanation of Local Revenues: (Revised) *Marion County COIT:* Under the bill, Marion County would be allowed to pass an ordinance to raise the County Option Income Tax (COIT) rate by 0.3% in a year. Assuming the County adopted an ordinance in 2005, a 0.3% rate increase in Marion County would generate an estimated $46.7 M in CY 2007. Under current law, a county that adopts COIT initially adopts at a 0.2% rate with an automatic yearly increase in the rate of 0.1% until the county reaches a rate of 0.6%. After reaching 0.6%, the county has the option to adopt another ordinance to further increase the rate by 0.1% per year until reaching the maximum allowable rate of 1.00%.

Impact to Marion County COIT Revenue: Under current law, Marion County could increase their COIT rate by 0.1% for three successive years. (Under an ordinance adopted under current law, in year one, the County would receive an estimated $15.6 M (1/3 of $46.7 M) at an additional 0.1% rate. In year two, the County would receive approximately $31.1 M at an additional 0.2% rate. In year three, the County would receive approximately $46.7 M at a 0.3% rate.)

The following table exhibits the difference in the estimated revenue that could be received by Marion County under the proposal (0.3% rate increase in one year) against what Marion County could receive under an ordinance adopted under current law (0.1% rate increase per year for three successive years.)

Year	Additional Revenue Under Proposed One-Time Rate Increase of 0.3%	Additional Revenue Under Current Law by Successive 0.1% Annual Rate Increases	Additional Revenue Impact to Marion County COIT
Year 1	$46.7 M	$15.6 M	$31.1 M
Year 2	$46.7 M	$31.1 M	$15.6 M
Year 3	$46.7 M	$46.7 M	$0

Note: Totals may not sum due to rounding.

Background: Currently, Marion County has a 0.70% COIT rate and is receiving a certified distribution of $104,750,918 in CY 2005.

State Agencies Affected: Department of State Revenue.

Local Agencies Affected: Marion County; State Budget Agency.

Information Sources: State Budget Agency: Local option income tax collections data. OFMA Income Tax Databases, Tax Years 2000 & 2001; Internal Revenue Services, Statistics on Income, http://www.irs.gov/taxstats.

Fiscal Analyst: Jim Landers, 317-232-9869. Chris Baker, 317-232-9851.